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NITL Spring Policy Forum

Arlington, Virginia –April 19, 2005



# The Railroads and the Surface Transportation Board

- Created by ICC Termination Act of 1995
- Born out of the deregulation movement
- Residual economic regulation of the railroads
- Far smaller staff and scope of authority



# STB Mission

- Exclusive authority to approve of rail mergers
- Review rail rates and practices to ensure they are reasonable and not discriminatory
- Approval, including environmental review, of
  - (i) construction of any new rail line or
  - (ii) abandonment of existing lines
- Motor carrier collective ratemaking activities
- Rates for non-contiguous domestic water trade
- Rates for pipelines not carrying energy products



# STB Responsibilities over Rates and Service

- Oversee and monitor railroad practices nationally
- Enforce the railroads' common carrier obligation
- Ensure that rates charged captive shippers are reasonable
- Assist railroads in earning adequate revenues
- Calculate the railroads' cost of capital



# Rate Case Resolution

- Determination of Market Dominance
- Stand Alone Cost Test—*Fact-based approach rooted in economic reasoning and approved by the courts*
- No substitute for preparing a strong case with solid evidence
- Strive for a balance between railroad's need to earn
- Adequate Returns and Shipper's Need for Fair and Reasonable Rates



# Alternative Approaches

- SAC approach has been criticized as artificial and overly complex
- SAC approach is very costly and time consuming  
Only feasible for large shippers—no small shipper cases
- Is it time to look for alternative approaches?
  - Recent Board decisions suggest openness to proposed rulemaking on SAC changes
  - April 26th hearing on the SAC process



# Railroad Regulation and Capacity

- STB's Role has centered on rate reasonableness for regulated traffic
- Most commodities are exempt from regulation and/or modally competitive
- Interstate commerce laws and doctrine address reasonableness of rates and service
- Shippers want "Fairness"
- What can and should the Board do?



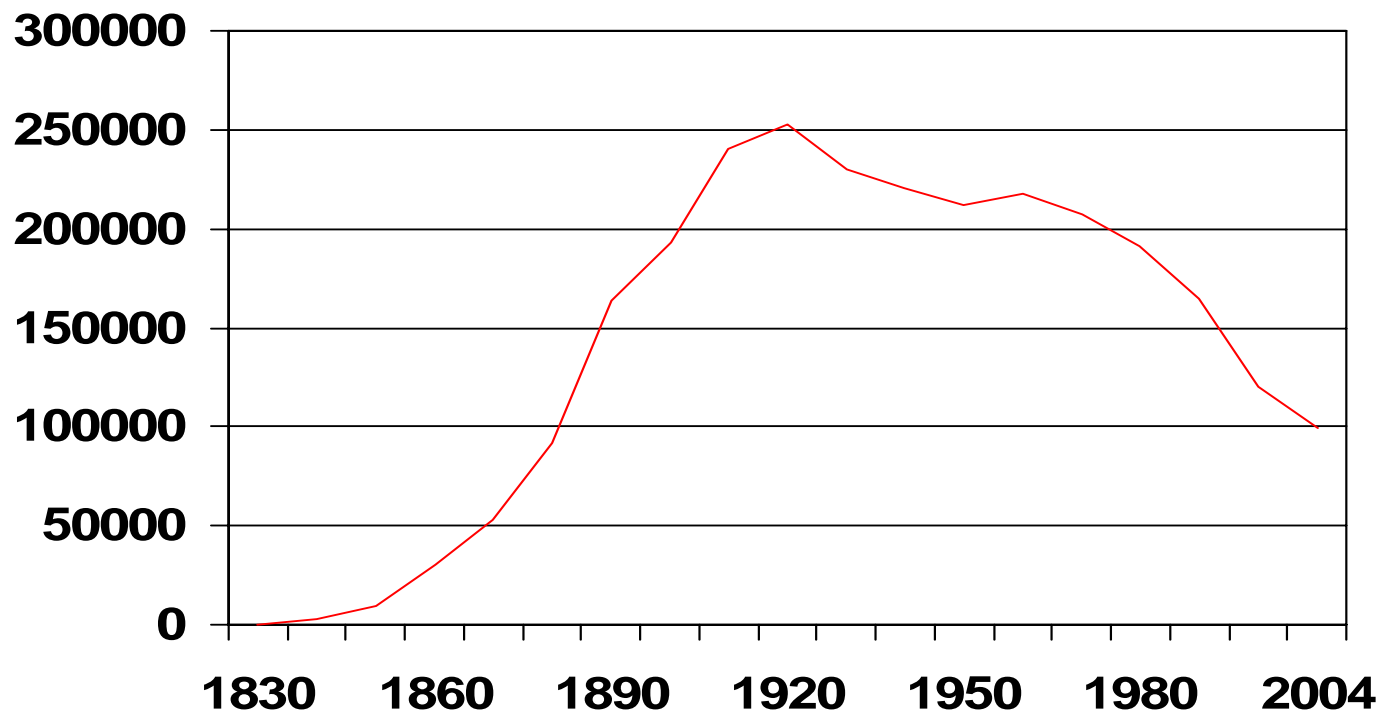
# The Railroads' Dilemma

- Improved earnings still not revenue adequate
- Railroads “Punished” by Wall Street for making capital investments
- Railroads often found that infrastructure investments
- Failed to generate sufficient income
- Long term strategy to reduce size of workforce
- Added rail infrastructure is long-lived while demand increases can be short-lived



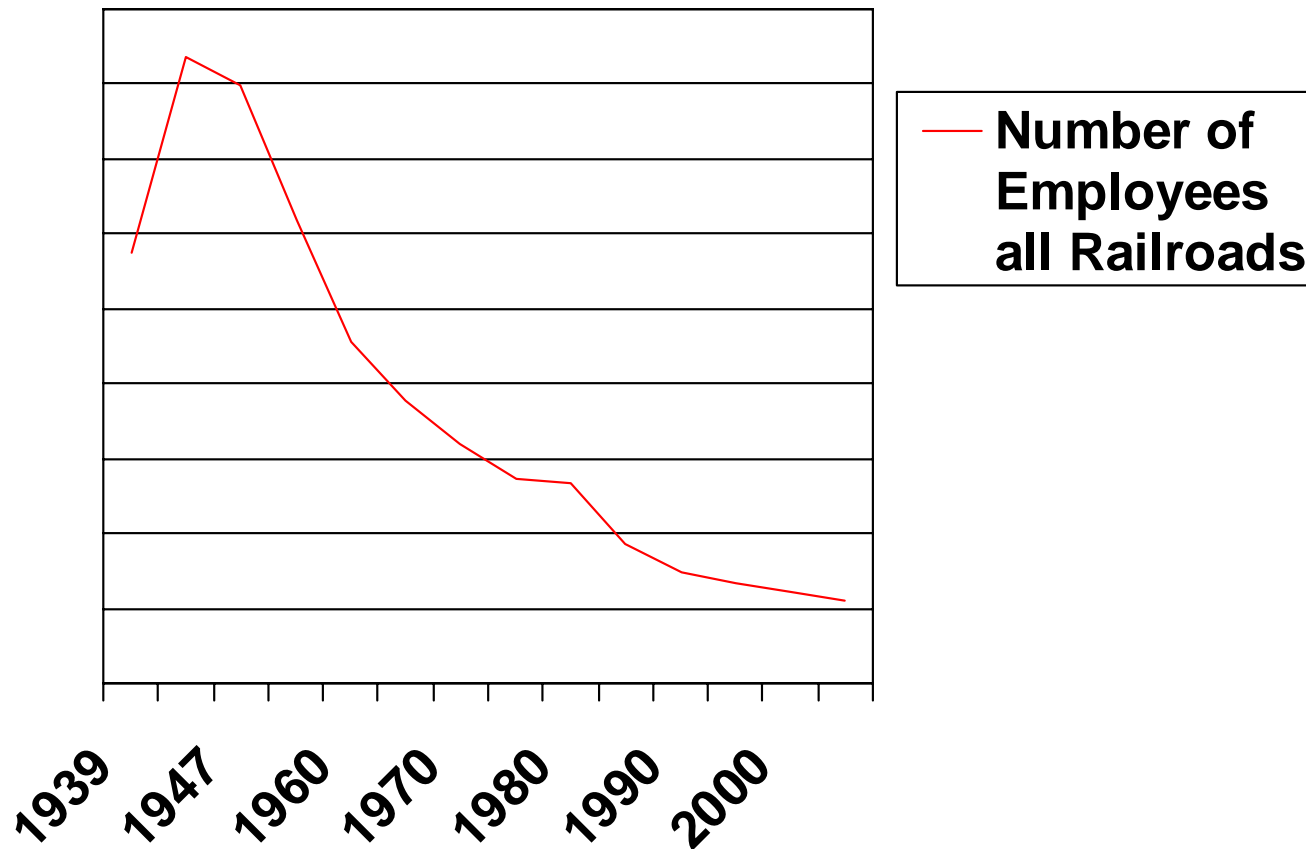


# Growth of Railroad Mileage



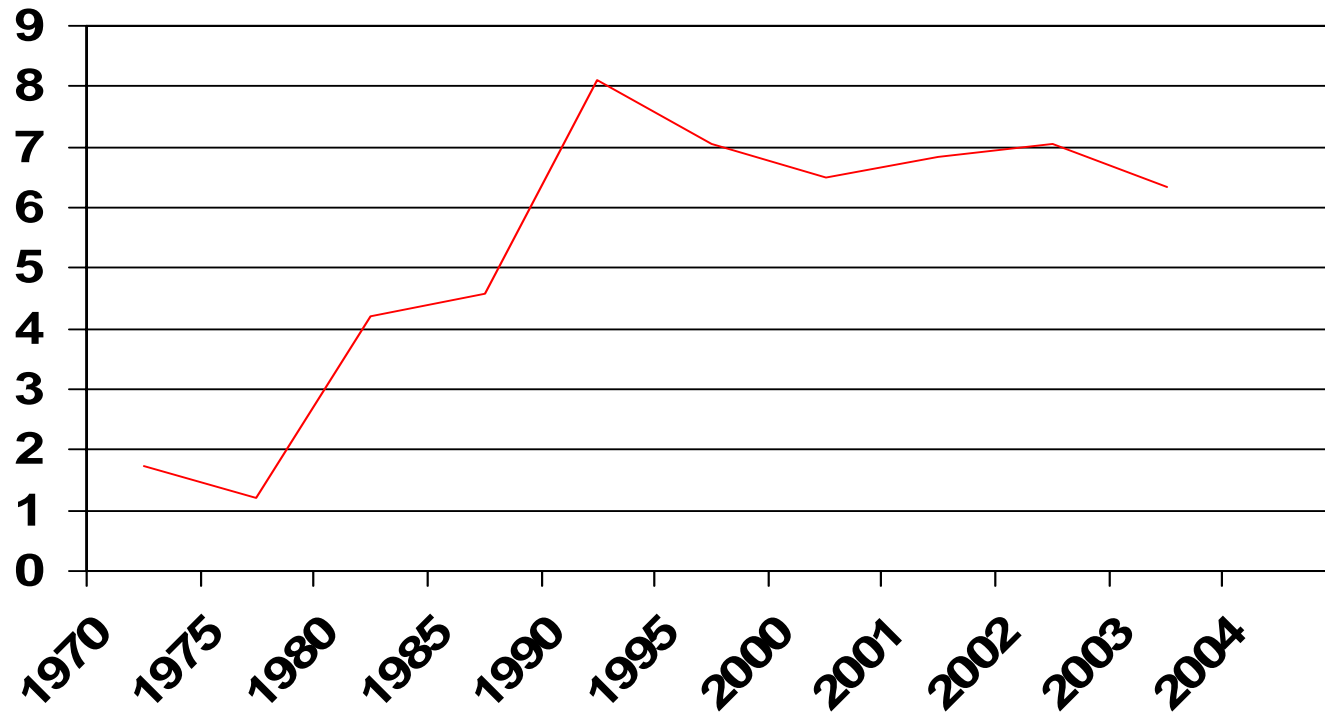
# Railroad Employment 1939-2003

(in thousands)





# Railroad ROI 1970-2003





# Railroad Cost of Capital and ROI

Sources: Annual R-1 Reports and AAR

	Cost Of Capital	BNSF	CSXT	NS	UP	KCS	SOO	GT	IC
1996	11.9%	8.6%	8.9%	13.0%	9.3%	7.2%	23.5%	0.0%	15.2%
1997	11.8%	8.4%	9.8%	13.1%	5.2%	3.6%	12.3%	5.2%	15.8%
1998	10.7%	9.7%	8.1%	10.5%	2.9%	9.1%	4.9%	3.0%	13.6%
1999	10.8%	9.5%	3.8%	5.2%	6.8%	6.4%	2.5%	25.4%	10.0%
2000	11.0%	8.8%	3.6%	5.5%	6.9%	6.3%	5.6%	5.9%	5.9%
2001	10.2%	7.1%	4.6%	8.3%	7.6%	7.0%	5.9%	4.9%	4.9%
2002	9.8%	6.4%	5.2%	9.1%	8.6%	6.5%	5.7%	3.1%	3.1%
2003	9.4%	6.2%	4.0%	9.1%	7.3%	3.7%	.01%	4.5%	4.5%



# The Developing Rail Capacity Crisis

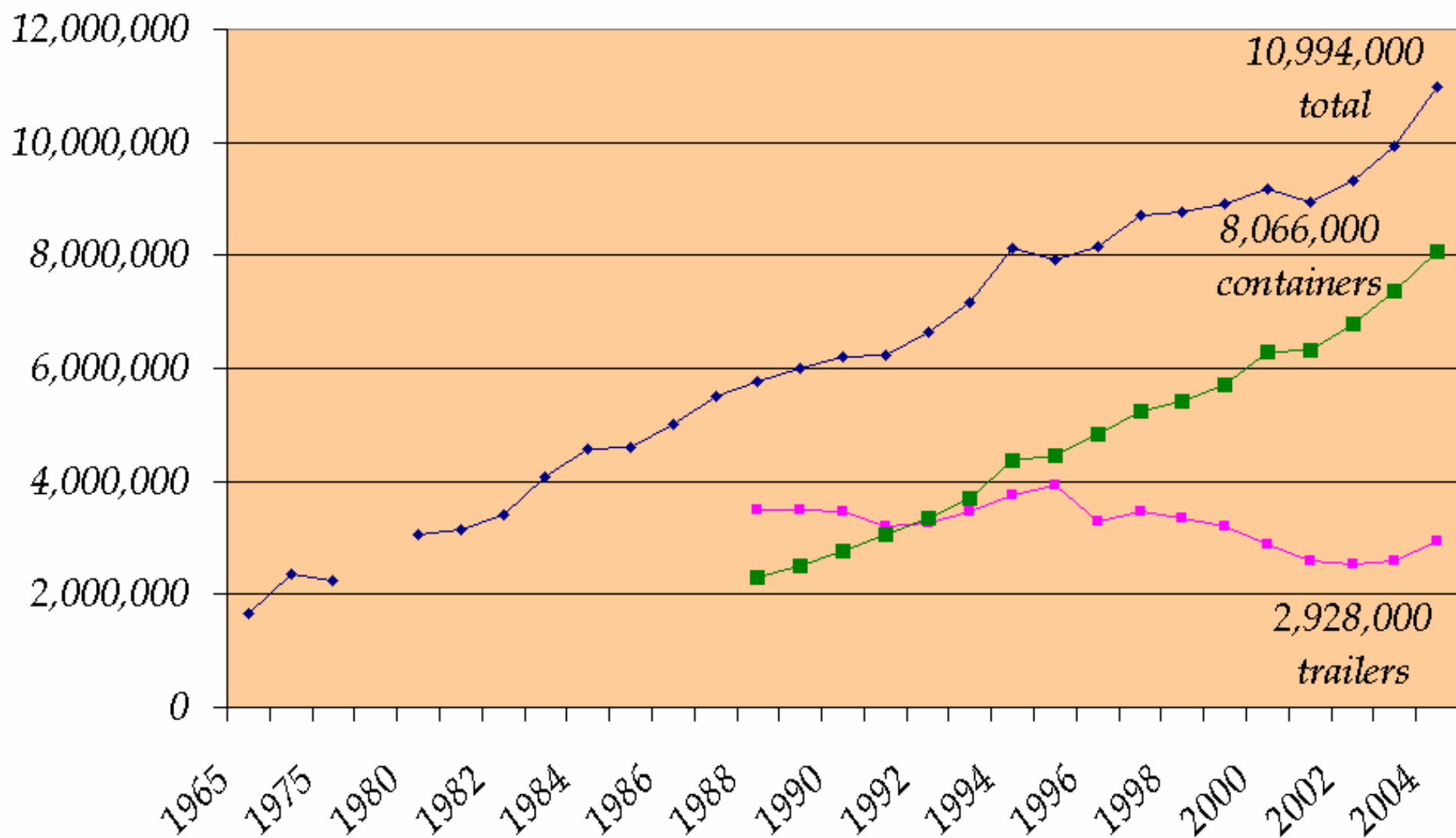
- Shrinking workforce and infrastructure partly offset by productivity improvements
- But continuous increase in traffic begins to absorb “Excess Capacity”
- Network becomes more vulnerable to stochastic events
- A perfect storm or the rail version of global warming



# Capacity Problems 2003-2004

- Expanding Economy Led to Surge in Imports
- Large Grain Harvests in 2003 and 2004
- Growth in Export Coal Market
- Crew Shortages due to Wave of Retirements
- Equipment Shortages due to Reduced Purchases

## *Intermodal Shipments beginning 1965*





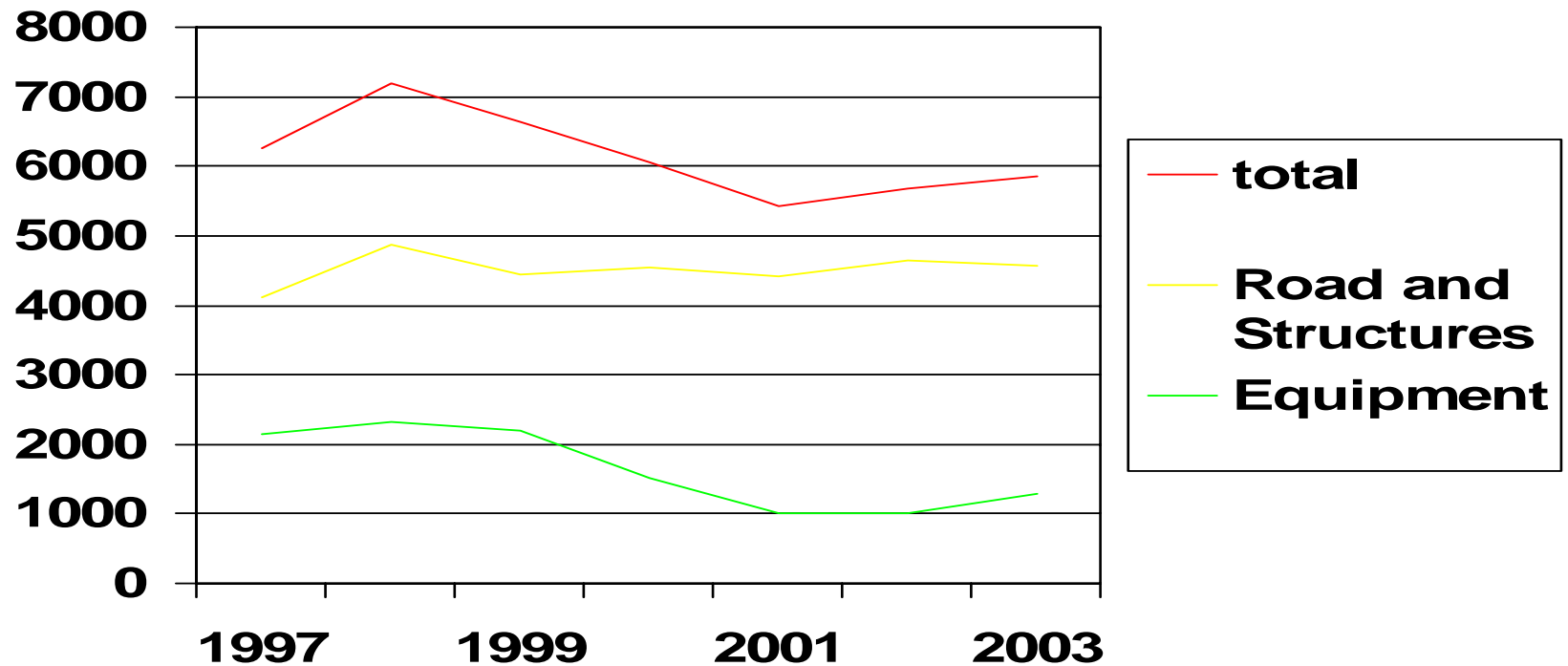
# Capacity Problem 2003-2004

- Cutbacks in Capital Spending Programs
- Tight capacity in trucking industry due to driver shortages, higher fuel costs, HOS rules, etc.
- A Perfect Storm?





# Class I Capital Expenditures (in billions of current \$)





# Carrier Responses to Recent Capacity Problem

- More cars and locomotives bought and leased  
accelerated hiring and training of train crews
- Some infrastructure expansion efforts
- Price rationing of available capacity
- Railroads choosing who they will serve and the  
Common Carrier Obligation



# Long-Term Rail Capacity Constraint Factors

- Demand for freight rail transport projected to grow by 60%-70% over next two decades
- Railroads' inability to earn cost of capital
- Pressure from Wall Street to reduce capital costs and improve ROI
- Long-Term contracts limit railroad pricing flexibility
- Railroads tend to bid long term contract
- Rates down to long run marginal costs



# What is The Role of the Public Sector?

- Railroads support limited Role—Public/Private Partnerships (Alameda Corridor, CREATE)
- Railroad trust fund concept
- Investment tax credits
  - Short Lines and the 286K lb. Car Problem
  - Class I Access and Limited Fiscal Capacity
  - RIM and RIFF



# Recent Changes in STB Procedures

- Greater openness, more public meetings
- Increased reliance on mediation and technical conferences
- Expedited discovery procedures
- Greater shipper and carrier outreach



## STB's Service Initiatives in 2004

- Board carefully monitored rail trends and performance metrics
- Urged open communication between railroads and shippers
  - San Francisco, Atlanta, Kansas City and Houston Service forum
  - Worked to resolve many smaller service complaints
- Asked railroads to submit their fall peak plans
- Worked with railroads and shippers on service issues



# STB – 2005 Priorities

- Progress on small rate cases
- Improved customer service from carriers
- Examination of capacity constraints
- Amtrak Directed Service Mandate



# Rail Consumer Assistance Program

- Facilitates informal solutions to disputes with RR's
- Brings issues to RR's attention rapidly
- Solves Problems without Litigation
- Promotes Rail Service Improvements
- 120 Rail Consumer complaints handled in 2004;  
over 420 handled since program began in 2000





# Is It Time to Review Rail Regulatory Policy?

- Focus on 25<sup>th</sup> Anniversary of Staggers Act and 10<sup>th</sup> Anniversary of the creation of the STB
- Proposed TRB study of railroads and regulation in the 21<sup>st</sup> Century

# Thank You, Any Questions?

